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Supreme Court of the United States.

OCTOBER TERM, 1940.

EVERETT WARE CADY ET AL., PETITIONERS,

v.

CLIFFORD J. MURPHY, RESPONDENT.

PETITION FOR A WRIT OF CERTIORARI TO THE CIRCUIT COURT OF APPEALS FOR THE FIRST CIRCUIT AND BRIEF IN SUPPORT THEREOF.

Petition.

To the Honourable the Justices of the Supreme Court of the United States:

The undersigned, on behalf of Everett Ware Cady, Alfred E. Thurber, W. Palmer Dixon, Hollis Hunnewell, Fred Zettler, E. Mauran Beals, Jr., Herbert N. Rawlins, Jr., Willis P. Beal, Arthur N. McGeoch, Jr., James Averell Clark, Henry Parish II, Alexander R. McKernan, Sidney B. Curtis, John Harsen Rhoades, and George Sloane, petitioners, pray that a writ of certiorari may issue to review the judgment of the Circuit Court of Appeals for the First Circuit entered August 15, 1940, in the case between the above-named parties, docketed therein as No. 3570, affirming the judgment of the District Court for the District of Maine, wherein the petitioners were defendants and the respondent plaintiff.

OPINIONS BELOW.

The opinion of the District Court (Rec. pp. 285-292) is published in 30 Fed. Supp. 466. The opinions in the Circuit

Court of Appeals (Rec. pp. 299-305) are published in 113 F. (2d) 988.

Jurisdiction.

The final judgment of the Circuit Court of Appeals was entered August 15, 1940 (Rec. p. 306).

The jurisdiction of this Court is invoked under Section 240(a) of the Judicial Code as amended, U.S.C. Title 28, Section 347.

The jurisdiction of the District Court was based upon diversity of citizenship.

Questions Presented.

The fundamental question presented is whether a stock-exchange firm which acts solely as broker for the purchaser of a security from whom by interstate telephone calls it has solicited an order to buy can be held liable as a seller of said security under Section 12(2) of the Securities Act for misrepresentations of fact regarding the security purchased.

There is likewise presented the question of practice whether, under the Rules of Civil Procedure, upon an appeal in a law action tried without a jury, it is competent for the Circuit Court of Appeals itself to make a finding of fact not made by the District Judge and to decide the case upon the basis of that finding.

Statute Involved.

Section 12 of the Securities Act of 1933 reads as follows:

"Sec. 12. Any person who—

"(1) sells a security in violation of section 5, or

"(2) sells a security (whether or not exempted by

the provisions of section 3, other than paragraph (2) of subsection (a) thereof), by the use of any means or instruments of transportation or communication in interstate commerce or of the mails, by means of a prospectus or oral communication, which includes an untrue statement of a material fact or omits to state a material fact necessary in order to make the statements, in the light of the circumstances under which they were made, not misleading (the purchaser not knowing of such untruth or omission), and who shall not sustain the burden of proof that he did not know, and in the exercise of reasonable care could not have known, of such untruth or omission,

shall be liable to the person purchasing such security from him, who may sue either at law or in equity in any court of competent jurisdiction, to recover the consideration paid for such security with interest thereon, less the amount of any income received thereon, upon the tender of such security, or for damages if he no longer owns the security."

Definitions of terms are found in Section 2, as follows:

"Sec. 2. When used in this title, unless the context otherwise requires . . .

"(3) The term 'sale', 'sell', 'offer to sell', or 'offer for sale' shall include every contract of sale or disposition of, attempt or offer to dispose of, or solicitation of an offer to buy, a security or interest in a security, for value; . . .

"(12) The term 'dealer' means any person who engages either for all or part of his time, directly or indirectly, as agent, broker, or principal, in the business of offering, buying, selling, or otherwise dealing or trading in securities issued by another person . . ."

The Circuit Court of Appeals was of the opinion that the following provisions of Sections 4 and 5 were pertinent to the decision of the case:

> "Sec. 4. The provisions of section 5 shall not apply to any of the following transactions:
>
> "(1) Transactions by any person other than an issuer, underwriter, or dealer; . . .
>
> "(2) Brokers' transactions, executed upon customers' orders on any exchange or in the open or counter market, but not the solicitation of such orders . . .
>
> "Sec. 5. (a) Unless a registration statement is in effect as to a security, it shall be unlawful for any person, directly or indirectly—
>
> "(1) to make use of any means or instruments of transportation or communication in interstate commerce or of the mails to sell or offer to buy such security through the use or medium of any prospectus or otherwise; . . ."

Statement of the Case.

The respondent is a small broker and dealer in securities doing business in Portland, Maine, under the style of "Clifford J. Murphy Co." The petitioners at all material dates were members of the stock-brokerage firm of Rhoades & Company carrying on a general brokerage business with offices in New York and Boston. They likewise maintained a branch office in Portland and through that had had numerous dealings with the respondent over a period of years (Rec. pp. 10-12).

In the late winter of 1937 one Lynch, a trader in the petitioners' Boston office, by telephone to Portland recommended to the respondent a stock subsequently identified

as South American Utilities. In the course of the recommendations which he made to the respondent, Lynch made statements which unquestionably were not in accord with the facts and which he might have ascertained were not true. There was a clear split in testimony between Lynch and the respondent as to whether these statements were made as statements of fact or as specifically designated repetition of hearsay information received by Lynch. The judge found on sufficient evidence that the respondent was justified in accepting them as being made as statements of fact (Rec. p. 288) and the petitioners make no contention here that these representations would not have supported recovery in the event that Section 12(2) of the Securities Act applied to the case.

Early in March, 1937, the respondent purchased 1700 shares of the stock at the price of $4.50 per share. It was stipulated by the parties that the 1700 shares were part of a block of 1970 which Lynch ordered by means of one telephone conversation between Boston and New York (Rec. p. 281). The stock was purchased from E. E. Smith & Co., a small unlisted dealer in New York. The petitioners' records show that the 1700 shares were purchased by the petitioners as brokers for the account of the respondent (Exh. 5a, Rec. p. 257; Exh. H, Rec. p. 275). The petitioners charged the respondent a commission of four cents a share, or $68 (Exh. C, Rec. p. 270, and Exh. H, Rec. p. 275). From this the petitioners paid a clearance fee of two cents, so that their net profit and sole gain on the transaction was $34 (Rec. pp. 134, 135).

The parties were sharply at issue as to whether the telephone conversation at which the respondent admittedly ordered the 1700 shares took place on March 1 or March 3, 1937. The respondent drew his writ (Rec. pp. 2-4) and tried his case upon the theory that the petitioners were acting as principals and not as brokers. His contention that

the conversation took place on March 3 was urged to show that they were acting as principals. On this issue the trial judge found and stated in his opinion:

> "For the benefit of the defendants I will say that the evidence is not sufficient to satisfy me that the defendants owned this stock and sold it as principals" (Rec. p. 290).

In fact, the intrinsic value of the stock was materially less than the $4.50 per share which the respondent paid for it, and not long after the purchase it declined on the market. The respondent then tendered it back to the petitioners and demanded a return of the money he had paid. The tender was refused and the action was brought in the District Court for the District of Maine as a common-law action on the case (under the old practice), commenced by writ dated October 6, 1937 (Rec. p. 36). Subsequently the respondent disposed of most of the stock for less than he had paid. The declaration (Rec. pp. 2-4) contained one count at common law for deceit and three counts under Section 12(2) of the Securities Act of 1933.

The trial judge found and ruled for the petitioners on the common-law count, so no question is presented with reference to it.

On the counts under the Securities Act the respondent offered evidence attempting to show that the stock was sold by the petitioners as owners. He likewise contended that, even though the petitioners acted as brokers, the Securities Act would apply and justify recovery. The petitioners insisted that they acted solely as brokers for the respondent and that under a proper construction of the act it gave no cause of action to a customer against his broker. There was no dispute between the parties that, if the petitioners were owners of the stock, the statute would apply, and no

contention was made that the petitioners had acted as brokers for E. E. Smith & Co., who had owned the stock before the transaction of March 1. The sole issue of law was whether Section 12 could apply when in fact the petitioners had acted as brokers for the respondent. As stated above, the judge did not find that the petitioners had acted as principals. On this sole issue of law he construed the word "sell" in Section 12 in the broadest manner possible, and proceeded to rule:

> "Whether the seller, being a broker, himself owns the security, or whether he is acting as the agent for the owners, or for the purchaser, or for both, is immaterial" (Rec. p. 291).

He consequently denied the petitioners' seventh and eighth requests for rulings, which read:

> "7. Section 77(l) of Title 15, U.S.C.A. (Section 12 of the Securities Act of 1933) has no application, except as between the vendor of a security and the vendee.
>
> "8. Said section has no application to the case where the plaintiff is a purchaser of securities and the defendant has acted merely as his broker" (Rec. p. 284).

Judgment was entered for the respondent (Rec. p. 293) and the petitioners appealed to the Circuit Court of Appeals.

That court affirmed the judgment of the District Court, but it did so upon a finding of fact made by it and not by the District Judge. The majority opinion quoted the ruling of the trial judge set out above as to the immateriality of the relationship, and said:

> "We need not decide whether Section 12(2) applies to the case of a broker acting solely for a purchaser, where the broker makes misrepresentations in the course of soliciting from the purchaser an order to buy.

> Even if the version of the defendants' witness Lynch is accepted, Rhoades & Company was acting either as agent for the seller or in a dual capacity as agent for both parties, in either of which cases Section 12(2) is applicable" (Rec. p. 304).

The District Judge had not found that the petitioners were acting as agent for the seller or in any dual capacity. No contention had been made to that effect, either at the trial or prior to the conclusion of the oral argument before the Circuit Court of Appeals. In that court a brief had been filed by an *amicus curiae* in which the sole argument made was that a person acting solely as broker for the purchaser could not come within the statute. In a reply to this brief, filed a fortnight after the conclusion of the oral arguments, the respondent for the first time advanced the contention that the petitioners had acted as agents for E. E. Smith & Co., the owner of the stock. This contention thus advanced was adopted by the majority of the Circuit Court of Appeals and was embodied in Judge Magruder's opinion as an essential finding of fact.

Judge McLellan, in a dissenting opinion, held that—

> "There was abundant evidence, which would have justified, if it did not require, a finding that the defendant acted not as agent for the seller but as agent for the plaintiff who was the buyer"—

and went on to say:

> "To me, it seems, that one who acts solely as agent for the purchaser cannot be regarded as a seller and that the liability of such an agent for misrepresentations rests upon common law principles, not upon the Securities Act which relates to misrepresentations by a seller.

"The trial judge having proceeded upon a contrary view, I think justice requires that the judgment of the District Court be set aside and a new trial ordered" (Rec. p. 305).

Specification of Errors.

The Circuit Court of Appeals erred:

1. In affirming the judgment of the District Court entered upon a ruling of law by the District Judge to the effect that Section 12(2) of the Securities Act of 1933 could give a cause of action to a purchaser of securities against his own broker.

2. In making a finding of fact in an action at law tried before a judge sitting without a jury, which finding was not made by the trial judge and which finding was essential to the affirmance of the judgment upon the legal theory adopted by the Circuit Court of Appeals in affirming the judgment.

3. In refusing to grant a new trial where the order for judgment of the trial judge was based upon a ruling erroneous upon a material particular.

4. In affirming the judgment of the District Court.

Reasons for Granting the Writ.

(1) The Circuit Court of Appeals so far departed from the accepted and usual course of judicial proceedings as to call for an exercise of this Court's power of supervision. The action was upon the law side of the court. The District Judge refused to find that the petitioners sold the stock in question to the respondent as principals. He ruled as a matter of law that it was immaterial whether the petitioners acted as brokers for the respondent, or for the owner of the stock, or both. He made no finding that the petitioners'

agent acted in any manner "as agent for the seller or in a dual capacity as agent for both parties." The case was not tried in the District Court or argued before the Circuit Court of Appeals on any issue of whether the petitioners' agent was acting for the seller. The Circuit Court of Appeals prompted by respondent's reply to the brief of the *amicus* made a finding of fact not made by the District Judge and decided the case solely upon the basis of this finding and refused to consider the issue of law tried in the District Court and argued before the Circuit Court of Appeals. There is no provision in the Rules of Civil Procedure which purports to give additional fact finding powers to the Circuit Courts of Appeals not vested in those courts before the adoption of the Rules of Civil Procedure. There is no reported case in which a Circuit Court of Appeals in a civil action in the nature of an action at law tried without a jury has itself made a finding of fact not made by the District Judge and has affirmed a judgment upon the basis of that finding. The reported decisions in the several circuits leave in doubt whether under the new rules such an action is open *de novo* in the Circuit Court of Appeals. This practice point is of great importance and should now be settled by the opinion of this Court.

(2) The issue presented in the case involves the decision by a divided Circuit Court of Appeals of an important question of federal law which has not been but should be settled by this Court. Prior to the decisions in this case no court had passed upon the question of whether the provisions of Section 12(2) of the Securities Act of 1933 imposed liability upon a party acting solely as a broker for the purchaser. The statute imposes a new and onerous liability in connection with sales of securities. It is important in the interests of dealers in securities that the scope of this liability should be authoritatively settled and this can be done only by a decision of this Court. The decision of the District Court

is direct authority that a broker soliciting an order to purchase from his own customer and executing for him the order thus obtained comes within the scope of the statute. The majority opinion of the Circuit Court of Appeals refuses to consider this point. The dissenting opinion of Judge McLellan construes the statute as not applying to such a situation.

The result of the three opinions is to leave the state of the law on this important point in grave doubt. By settling it at this time in this case this Court may administer prophylactic justice to buyers and sellers of securities generally.

The practical importance of this decision to the entire brokerage profession is evident and is manifested by the fact that the Boston Association of Stock Exchange Firms filed a brief in the Circuit Court of Appeals as *amicus curiae*. The decision of the Circuit Court of Appeals has also been made the subject of a special article appearing in the Wall Street Journal for Tuesday, September 3, 1940, and of special releases of the Securities and Exchange Commission dated August 30, 1940, in which the Securities and Exchange Commission assert that the Circuit Court of Appeals for the First Circuit "rendered an opinion under section 12 (2) of the Securities Act of 1933 holding that a broker *acting as agent for the seller of securities* was liable to the purchaser for misrepresentations made in the sale." (Italics supplied.)

Prayer.

Wherefore your petitioners respectfully pray that a writ of certiorari be issued out of and under the seal of this Court directed to the Circuit Court of Appeals for the First Circuit commanding said court to certify and send to this Court on a day certain to be therein designated a full and complete transcript of the record and all proceedings of the

said Circuit Court of Appeals in this case which was entitled in that court: *Everett Ware Cady et al., doing business under the firm name and style of Rhoades & Company, Defendants, Appellants,* v. *Clifford J. Murphy, doing business under the firm name and style of Clifford J. Murphy Co., Plaintiff, Appellee,* No. 3570, to the end that said cause may be reviewed and determined by this Court as provided by Section 240 of the Judicial Code as amended (U.S.C. Title 28, § 374), and that your petitioners may have such other and further relief or remedy in the premises as to this Court may seem appropriate and that the said judgment of said Circuit Court of Appeals in the said case may be reversed by this Honourable Court and your petitioners will ever pray.

EVERETT WARE CADY,
ALFRED E. THURBER,
W. PALMER DIXON,
HOLLIS HUNNEWELL,
FRED ZETTLER,
E. MAURAN BEALS, JR.,
HERBERT N. RAWLINS, JR.,
WILLIS P. BEAL,
ARTHUR N. McGEOCH, JR.,
JAMES AVERELL CLARK,
HENRY PARISH II,
ALEXANDER R. McKERNAN,
SIDNEY B. CURTIS,
JOHN HARSEN RHOADES, AND
GEORGE SLOANE,
By RICHARD WAIT,
ROBERT HALE,
Counsel for Petitioners.

Dated October 17, 1940.

STATE OF MAINE, }
CUMBERLAND, } ss.

Robert Hale, being duly sworn, says that he is counsel for Everett Ware Cady, Alfred E. Thurber, W. Palmer Dixon, Hollis Hunnewell, Fred Zettler, E. Mauran Beals, Jr., Herbert N. Rawlins, Jr., Willis P. Beal, Arthur N. McGeoch, Jr., James Averell Clark, Henry Parish II, Alexander R. McKernan, Sidney B. Curtis, John Harsen Rhoades and George Sloane, the petitioners herein; that he prepared the foregoing petition and that the allegations thereof are true as he verily believes.

ROBERT HALE.

Sworn to and subscribed before me, this 17th day of October, 1940.

LEON V. WALKER, JR.,
Notary Public.

Brief in Support of the Petition.

STATEMENT.

Statements regarding the opinions of the court below, the jurisdiction of this Court, the questions presented, and the errors assigned, will be found in the petition. The petition also contains a brief statement of the material facts.

SUMMARY OF THE ARGUMENT.

I. The scope of review by the Circuit Courts of Appeals following the adoption of the new rules should now be determined by this Court.

II. Section 12(2) of the Securities Act does not apply to brokers executing orders for their customers who purchase securities.

A. The petitioners are not "sellers" within the meaning of Section 12.

B. The respondent did not purchase the securities from the petitioners.

C. Section 12 contemplates rescission, impossible here.

D. Section 12 must be strictly construed.

I. THE SCOPE OF REVIEW BY THE CIRCUIT COURTS OF APPEALS FOLLOWING THE ADOPTION OF THE NEW RULES SHOULD NOW BE DETERMINED BY THIS COURT.

The Circuit Court of Appeals in affirming the judgment of the District Court did so upon a construction of Section 12(2) of the Securities Act imposing the liabilities of a seller upon a person acting as broker for the seller. The District Judge had made no finding to the effect that the petitioners had acted as brokers for the seller. The Circuit Court of Appeals, however, concluded from a short excerpt from Lynch's testimony (see Rec. pp. 127, 128, 302) that the

petitioners were acting as brokers for the seller. In other words, it, itself, made the focal finding upon which it affirmed the judgment below.* It could properly have done so only in the event that on the appeal the case was open *de novo* for the purpose of making findings not made by the District Judge.

Prior to the adoption of the new federal Rules of Civil Procedure, no possible justification could have been found for any such action by a Circuit Court of Appeals. If a law action can be open for new findings on appeal, it is only by virtue of the provisions of the new rules.

Except in so far as they may be abrogated by the new rules, trials of law cases in the District Court without the intervention of a jury and appeals from judgments in such cases are governed by the provisions of Title 28, U.S.C. §§ 773 and 875. Section 773 provides:

> "Issues of fact in civil cases in any district court may be tried and determined by the court, without the intervention of a jury, whenever the parties, or their attorneys of record, agree to waive a jury by a stipulation in writing filed with the clerk or by an oral stipulation made in open court and entered in the record. *The finding of the court upon the facts, which may be either general or special, shall have the same effect as the verdict of a jury.*"

*The Circuit Court of Appeals apparently gave no consideration to the documentary evidence. The petitioners' records clearly showed that they acted as brokers only for the respondent. Plaintiff's Exhibit 5a showed (at Rec. p. 257) the confirmation by the petitioners of the purchase from E. E. Smith & Co. for the account of the respondent, and at page 260 the confirmation of the sale by E. E. Smith & Co., which would not have been done had the petitioners been acting for E. E. Smith & Co. Similarly, Defendants' Exhibit C (Rec. p. 270) and Exhibit H (Rec. p. 275) showed the purchase of the securities for the account of the respondent. The respondent paid the petitioners a commission, and that was the only compensation which the petitioners received (Rec. p. 186).

Section 875 deals with review by the Circuit Court of Appeals in cases tried without a jury. This section provides:

> "When an issue of fact in any civil cause in a district court is tried and determined by the court without the intervention of a jury, according to section 773 of this title, the rulings of the court in the progress of the trial of the cause, if excepted to at the time, and duly presented by a bill of exceptions, may be reviewed upon a writ of error or upon appeal; *and when the finding is special the review may extend to the determination of the sufficiency of the facts found to support the judgment.*"

The only new rule which could possibly be deemed to amend these statutes by implication is Rule 52(a), entitled "Findings by the Court," and providing:

> "*Effect.* In all actions tried upon the facts without a jury, the court shall find the facts specially and state separately its conclusions of law thereon and direct the entry of the appropriate judgment; and in granting or refusing interlocutory injunctions the court shall similarly set forth the findings of fact and conclusions of law which constitute the grounds of its action. Requests for findings are not necessary for purposes of review. Findings of fact shall not be set aside unless clearly erroneous, and due regard shall be given to the opportunity of the trial court to judge of the credibility of the witnesses. The findings of a master, to the extent that the court adopts them, shall be considered as the findings of the court."

Of this the only part which is pertinent to the present case is the third sentence, reading:

> "Findings of fact shall not be set aside unless clearly erroneous, and due regard shall be given to the oppor-

tunity of the trial court to judge of the credibility of the witnesses."

This sentence is an exact statement of the well-established rule of practice in equity by which appellate courts limit the exercise of their undoubted power to consider the evidence in equity cases on appeal *de novo*. By incorporating this sentence in Rule 52, was it intended to enlarge the powers of Circuit Courts of Appeals beyond what they had previously been?

The language of Rule 52 alone discloses no intention to make any such radical change of practice. Nowhere is it stated that the evidence shall be open for review *de novo* by the appellate court. A statement that a finding of fact shall not be set aside unless clearly erroneous is not an apt way of saying that the appellate court shall have untrammeled power to make findings of fact not made by the trial court. This is particularly true where such a provision would effect the supersession of a statute which has long been on the books.

The notes of the Advisory Committee with reference to this rule do not suggest that it effected any such radical change in the practice. In those notes it is stated:

> "The provisions of U.S.C. Title 28, §§773 . . . and 875 . . . are superseded in so far as they provide a different *method* of finding facts and a different *method* of appellate review. The rule stated in the third sentence of subsection (a) accords with the decisions on the scope of the review in modern federal equity practice. It is applicable to all classes of findings in cases tried without a jury. . . ."

This statement is clearly indicative that the committee did not intend a complete change in the practice. It will be observed that they do not say that Sections 773 and 875 are

superseded *in toto,* but that they are superseded only in so far as they provide for a different *method* of making findings and of appellate review. A complete change in the scope of permissible review is far more than a change which provides a "different method of appellate review." "Method" obviously refers to the taking of exceptions in court, the presentation of requests for findings, the filing of a bill of exceptions, assignments of error, and the like. These things have been changed and a statement that the "method of appellate review" has been changed is an apt reference to them. Moreover, unless the provisions in Sections 773 and 875 which are italicized above still remain in force, the sections would have been superseded *in toto.* If they do remain in force, as we contend, the Circuit Court of Appeals exceeded its power in making the additional finding of fact which it made.

The question has not been considered by this Court. This Court has, however, indicated the requirement that essential findings be made by the trier of fact even where issues of fact are open to review in the appellate court.

Ford Motor Co. v. *Nat'l Labor Relations Board,* 305 U.S. 364:

In that case the Circuit Court of Appeals had remanded the case to the Board with directions that it should, among other things, issue proposed findings of fact. In commenting upon this point this Court said:

> "It is familiar appellate practice to remand causes for further proceedings without deciding the merits, where justice demands that course in order that some defect in the record may be supplied. Such a remand may be made to permit further evidence to be taken or additional findings to be made upon essential points. So, when a District Court has not made findings in accordance with our controlling rule (Equity Rule 70½)

it is our practice to set aside the decree and remand the cause for further proceedings" (p. 373).

From this it is apparent that, even had the instant case been in equity, the practice approved by this Court would have required the Circuit Court of Appeals to send the case back to the District Court for a finding rather than to make one itself on the issue as to whose brokers the petitioners were.

We have found no case in which a Circuit Court of Appeals has stated that the facts are open *de novo* on appeals in law cases. The courts in all of the circuits except the second and fifth have had occasion to refer to Rule 52(a) in law cases, but none has rendered a decision which would support the action taken in the instant case. On the contrary, there is substantial authority contra.

The court for the Seventh Circuit has stated flatly that the rule does not open the evidence *de novo*.

Webb v. *Frisch*, 111 F. (2d) 887, 888:

"We do not understand that the foregoing rule has enlarged the discretion of this court in passing upon the probative force of evidence. Our function is to review the finding of the lower court and not to pass upon the evidence de novo. We cannot say that a finding of the fact of prior use is 'clearly erroneous' merely because we might have entertained some doubt about the quantum of evidence. We must attach to the testimony of witnesses the full weight and quality of credibility which the trial court gave it."

Knapp v. *United States*, 110 F. (2d) 420, 422:

"The question of law we are asked to decide is whether the finding of the trial court was based upon substantial evidence. We are not the triers of fact but merely the reviewers of the action of the triers and

limited in our investigation to an ascertainment of the existence of substantial evidence sufficient to support the finding, . . . and in the consideration of this question we must assume as established all the facts that the evidence reasonably tends to prove . . . and the finding should not be set aside unless clearly erroneous."

See also *In Re Duvall,* 103 F. (2d) 653:

That was a bankruptcy case and so presented a somewhat different situation, but the following statement in the opinion (at p. 655) is illuminating:

"The argument presented here indicates that counsel, erroneously, we think, have assumed that this is a trial de novo. Ordinarily, this court sits merely in the capacity of review and is bound by the finding of the lower court where the same is supported by substantial evidence, notwithstanding the fact that we might have reached a different conclusion on a matter submitted to us as an original proposition. This situation, applicable to reviewing courts generally, is due to the long recognized fact that the court who has seen and heard the testimony of witnesses is in a better position to judge of their credibility and the weight to be attached to their testimony, than is a reviewing court with nothing before it but the printed record."

In the Ninth Circuit one of the Circuit Judges has clearly indicated that in his opinion the facts are not open *de novo* in a civil action in the nature of an action at law.

Occidental Life Insurance Company v. *Thomas,* 107 F. (2d) 876:

Here a judgment for the plaintiff on an insurance policy was affirmed after a consideration of the evidence support-

ing the finding of the District Judge. In a concurring opinion, Circuit Judge Haney stated:

> "I believe that the conclusion of the majority is reached by weighing the evidence, and doubt that we have any such power. I think it was for the trial court to determine whether the weight of the evidence was for appellee, for appellant, or whether the evidence gave equal support to each of two inconsistent inferences within the rule announced in Pennsylvania R. Co. v. Chamberlain, 288 U.S. 333, 339, 53 S. Ct. 391, 77 L. Ed. 819. Questions as to the weight of the evidence are not to be decided by us. The only question before us is whether or not the finding of the trial court is clearly erroneous. Federal Rules of Civil Procedure, Rule 52(a). I think such finding is clearly erroneous only if no reasonable man could logically infer accidental death from the evidence. I believe it is apparent that reasonable men would differ in making inferences from the evidence before us, and therefore the finding is not clearly erroneous. For these reasons I think the judgment should be affirmed" (p. 879).

The Circuit Court of Appeals for the First Circuit has intimated that the latitude of review on the facts has been somewhat enlarged by Rule 52.

Manning v. *Gagne,* 108 F. (2d) 718:

It was there stated (at p. 719):

> "The trial was without jury, and in such cases, the 'substantial evidence' rule no longer applies. By virtue of the Federal Rules of Civil Procedure . . . the applicable test is whether having due regard to the opportunity of the trial court to judge of the credibility of witnesses the finding was 'clearly erroneous', Rule 52(a)."

This is the furthest that any court has gone, and in this there is no suggestion that the Circuit Court of Appeals is empowered to do more than set aside a finding of the District Judge if clearly erroneous, even though there may have been substantial evidence to support it. Even if this is good law, it would not justify the action of the court in the instant case. It is interesting to note that the court in the *Manning* case spoke through Judge McLellan, who dissented in the case at bar on the ground that there should have been a new trial.

It is pertinent in connection with the conclusion reached in the *Manning* case to consider a case from the Eighth Circuit.

Luzier's, Inc., v. *Nee*, 106 F. (2d) 130, 135:

> "It must be borne in mind that the court below was exercising the functions of a jury, and its findings are of the same force and effect as though the same were embodied in a jury's special verdict, 28 U.S.C.A. §773, and cannot be disturbed when there is substantial evidence tending to support the finding.
>
> "The trial court found that the tax involved herein was 'passed on' to the purchasers of the taxpayer's products. Were there some basis for concluding the contrary (we are of the opinion there is none), it is not within the province of this Court to re-examine the evidence and reverse this finding, unless the same is clearly wrong. It was the trial court's duty and right to determine the preponderating weight of the evidence. See United States v. Jefferson Electric Manufacturing Company, supra.
>
> "This Court, in Brooks v. Willcuts, 8 Cir., 78 F. 2d 270, on page 273, expressed itself on the question in the quotation from Dooley v. Pease, 180 U.S. 126, page 131, 21 S. Ct. 329, 45 L. Ed. 457, as follows:

"'Where a case is tried by the court, a jury having been waived, its findings upon questions of fact are conclusive in the courts of review, it matters not how convincing the argument that upon the evidence the findings should have been different. Stanley v. Supervisors, 121 U.S. [535] 547, 7 S. Ct. 1234, 30 L. Ed. [1000] 1002.

"'Errors alleged in the findings of the court are not subject to revision by the circuit court of appeals, or by this court, if there was any evidence upon which such findings could be made [citing cases].'

"We are bound by this finding unless the same is clearly erroneous. Federal Rules of Civil Procedure, No. 52, 28 U.S.C.A. following section 723c; Collier v. Union Central Life Insurance Company, 5 Cir., 100 F. 2d 411; Guilford Const. Company, et al., v. Briggs, 4 Cir., 102 F. 2d 46."

The cases in the Eighth Circuit are of some interest, since that is the only court which has reversed the trial court on an issue of fact. It did so in

New York Life Insurance Company v. *Stoner*, 109 F. (2d) 874

and

State Farm Mutual Automobile Insurance Co. v. *Bonacci*, 111 F. (2d) 412.

Both of these cases were proceedings for declaratory judgments and it is not clear whether they were of equitable or of legal nature. In the *Bonacci* case, however, the court stated that Rule 52(a) "contemplates a review by the appellate court of the sufficiency of the evidence to sustain the findings" (p. 415). It made no suggestion that the evidence was open *de novo* for findings not made by the trial judge. In the *Stoner* case Judge Van Valkenburgh in his

concurring opinion pointed out that in the judgment of the court there was no room for disagreement as to the weight of the evidence, and went on to say:

> "It being the judgment of the majority that the evidence in favor of appellant leaves no disputed question for the trier of the facts, Rule 52 of the Rules of Civil Procedure is without application" (p. 884).

This is a clear suggestion that Rule 52 does not open the evidence to consideration *de novo*.

There are numerous other cases in which the courts have referred to the rule, but the references are not particularly illuminative either way.*

A radical change in practice accomplished through the implied repeal of ancient statutes by the promulgation of a new rule should require the opinion of this Court. The decision of the Circuit Court of Appeals, if it stands, how-

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Third Circuit:
Automobile Insurance Co. v. *Springfield Dyeing Co.*, 109 F. (2d) 533.
Fourth Circuit:
United States v. *One Hudson Coupe*, 110 F. (2d) 300.
Seventh Circuit:
United States v. *Borg-Warner Corp.*, 108 F. (2d) 424.
McDaniel v. *United States*, 108 F. (2d) 450.
United States v. *Anderson*, 108 F. (2d) 475.
Eighth Circuit:
Columbia Insurance Co. v. *Peoples Exchange Bank*, 109 F. (2d) 530.
Ninth Circuit:
Anglo California National Bank v. *Lazard*, 106 F. (2d) 693.
Maryland Casualty Company v. *Stark*, 109 F. (2d) 212.
Young v. *United States*, 111 F. (2d) 823.
Tenth Circuit:
American Home Fire Assurance Co. v. *Hargrove*, 109 F. (2d) 86.
Creel v. *Hudspeth*, 110 F. (2d) 762.
Pers v. *Hudspeth*, 110 F. (2d) 812.

ever, will constitute flat authority to the effect that in a law case tried without a jury the evidence is open *de novo* on appeal. The point is manifest from the dissenting opinion. This important point of practice was not argued in the instant case and has not been foreshadowed in any other case decided by any Circuit Court of Appeals. Other decisions, as we have seen, are in conflict. It is our contention that no such change in the practice has been accomplished by the promulgation of the new rules. Certainly the point is one which should be settled by this Court.

II. Section 12(2) of the Securities Act does not apply to brokers executing orders for their customers who purchase securities.

A. The petitioners are not "sellers" within the meaning of Section 12.

The respondent framed his declaration (Rec. pp. 2-4) on the theory that the petitioners owned the 1700 shares of South American Utilities and sold them to the respondent as principals. This would have given him a clear right of recovery under Section 12 of the Securities Act, but he was defeated in this attempt by the finding of the District Judge, already referred to, that the evidence was not sufficient to show that the petitioners owned the stock and sold it as principals (Rec. p. 290).

The evidence will support no other conclusion than that the petitioners were brokers who, after recommending the purchase of the shares in question, accepted and executed the respondent's order for the purchase of the shares. It is conceded that the judgment below may be supported if, and only if, a broker who accepts and executes an order for the purchase of securities is liable to his customer as a "seller" within the meaning of the Securities Act. This

was the only question presented on the record to the Circuit Court of Appeals, but this question that court did not decide at all.

Taking the narrow point presented on this record, we seek a construction of the applicable language of Section 12, which, omitting words here irrelevant, reads:

> "Any person who . . . sells a security . . . by means of an . . . oral communication, which includes an untrue statement of a material fact . . . and who shall not sustain the burden of proof that he did not know . . . of such untruth . . . shall be liable to the person purchasing such security from him, who may sue . . . to recover the consideration paid for such security . . . or for damages if he no longer owns the security."

The petitioners here contend that they are not within the meaning of the foregoing words "persons who sell a security," that the respondent did not purchase the security "from them," and that the respondent cannot recover from them the "*consideration*" paid for the security, because they never received it. As the respondent could not recover the consideration from them, there is no reason why he should recover damages.

Obviously the purpose of Section 12 was to put an end to the common-law doctrine of *caveat emptor*. The burden which the common law placed squarely on the shoulders of the buyer was lifted by the statute and placed just as squarely upon the shoulders of the seller. Under the statute the buyer need not beware, he may be as credulous as he choose—the seller, on the other hand, speaks at his peril. That, however, is as far as the statute goes. It is concerned only with the relationship between buyer and seller. It does not purport to say that any person who makes a mis-

representation concerning a security shall be liable to any other person who suffers loss as a consequence. It only says that a person who *sells* and misrepresents shall be liable to the person who *purchases from him.*

The relationship on which the liability depends is stated perfectly clearly and without the slightest ambiguity. The eligible defendant is defined as "any person who . . . *sells* a security" and the eligible plaintiff as "the person purchasing such security *from him.*" Persons occupying any other relationship could not qualify.

For example, suppose that a credulous investor purchases a security on the recommendation of a careless investment counsellor who has misstated the facts. The result may be that the investor loses his money, but he would have no cause of action under the statute. The investment counsellor did not sell the security (although he was the active cause of the purchase) and the investor did not purchase the security from him (although he did purchase because of him). The requisite relationship of seller and buyer could not exist. Whatever might be the situation at common law, liability under the express language of the Act could arise only on the passage of title from defendant to plaintiff.

So here, Rhoades & Company did not sell the 1700 shares of South American Utilities to Murphy. Murphy did not purchase it from them. Rhoades & Company did not receive the consideration for the shares.

The District Judge, however, although he found that there was no true sale, concluded that the definition of the word "sell" in Section 2 of the Act was so broad as to make Section 12 applicable even in the absence of the seller-buyer relationship (Rec. pp. 290, 291). The language of Section 2 which he relied on is:

> "The term 'sale', 'sell', 'offer to sell', or 'offer for sale' shall include every contract of sale or disposition

of, attempt or offer to dispose of, or solicitation of an offer to buy, a security or interest in a security, for value."

From this he reasoned that, because Lynch had initiated the dealings and had recommended the stock to Murphy, he had made a "solicitation of an offer to buy" the South American Utilities stock and so was a "person who . . . sells a security."

This, it is submitted, strains the definition beyond its reasonable meaning. It is not unusual for someone who has something which he wishes to sell to approach a prospective purchaser and ask him to make an offer to buy. Such a request is not strictly an offer of sale, although it may result in a sale quite as much as a straight offer of sale. It is a part of the negotiation of the contract of sale and consequently is something reasonably to be included in the sort of definition contained in Section 2. The intent of Section 2 was to prevent a person who has sold a security from saying: "I never offered to sell, I got the buyer to make me an offer which I accepted. You cannot hold me on any offer." That section also is concerned with the seller-buyer relationship and it is designed to cover all aspects of that relationship, but no more.

Four terms are defined: (1) sale, (2) sell, (3) offer to sell, and (4) offer for sale. There are also four definitions: (1) contract of sale, (2) disposition of, (3) attempt or offer to dispose of, and (4) solicitation of an offer to buy. The two groups obviously are designed to be in balance and "solicitation of an offer to buy" is set against "offer for sale." The definition is designed to include every action which a seller could take through which title would pass from him to the buyer. It accomplishes this design, but it endeavours to do no more.

It may be that the decision of the District Judge arose from a confusion between the expressions "soliciting an offer to buy" and "soliciting an order to buy." What the broker ordinarily does with his customer is to solicit the customer's *order* to buy for the customer's account. This is not the same thing as soliciting an *offer* to buy. The only person who can truly solicit an *offer* to buy is the offeree or the offeree's agent, that is to say, the prospective vendor. A broker who solicits authority from a customer to buy a certain security for the latter's account is *not* a person who solicits an *offer* to buy a security. Of course in ordinary speech no one would think of saying that he had given an *offer* to buy a security to his own broker. What a customer who has decided to buy a security gives to his broker is an *order* to buy. Here what Rhoades & Company solicited from Murphy was an *order* to buy and *not an offer* to buy.

This does not mean, of course, that brokers may not solicit offers. It merely means that a broker does not solicit an offer to buy from his own customer. A broker who buys securities for a customer does not sell them, whether his authority to buy be solicited or not.

Apart from the statute this proposition is amply supported by authority. Note particularly *Gill* v. *Hornblower*, 294 Mass. 26.

In that case the applicable statute (Massachusetts General Laws [Ter. Ed.] c. 110A, sec. 2(d)) provided:

> " 'Sale' or 'sell' shall also include an attempt to sell, an option of sale, a solicitation of a sale, a subscription or an offer to sell, directly or by an agent, or by a circular, letter, advertisement or otherwise."

It was held that a broker to buy securities did not sell them within the meaning of the statute.

The Court said, in part:

> "In ordinary speech, the transaction in question would not be described as a 'sale' of stock by the defendants to the plaintiff's testatrix. Rather, the defendants were her agents to buy stock" (p. 28).

See also—

Campbell v. *Willis*, 290 Fed. 271, 274 (App. D.C.).
Markham v. *Jaudon*, 41 N.Y. 235, 244.
Fowler v. *N.Y. Gold Exchange Bank*, 67 N.Y. 138, 143.
Rice v. *Winslow*, 180 Mass. 500, 502, 503.
Chase v. *Boston*, 180 Mass. 458.
Post v. *Leland*, 184 Mass. 601.
Prince v. *Scura*, 272 N.Y.S. 362.

The nature of the act performed by a broker who buys for the account of a customer is, of course, in no way altered by the manner in which the broker obtained his authority, whether by solicitation or otherwise. If authority were bestowed without solicitation, it would not be claimed that the broker was a selling agent; it would be clear that he was an agent to buy only. But, if the broker does solicit his authority, does he cease to be a buying agent and become a selling agent only, for the purposes of the statute at least? Or is he both a buying and a selling agent, and, if so, does he as buying agent buy from himself as selling agent?

Such theoretical difficulties result because solicitation of an *order* to buy securities is treated as identical with solicitation of an *offer* to buy securities. When the natural distinction between the words is regarded, it is clear that one who solicits an *order* to buy does not sell.

It is not to be inferred that Congress used the words "order" and "offer" interchangeably and without recognizing any difference in meaning.

B. The respondent did not purchase the securities from the petitioners.

Furthermore, applying the definition of Section 2 to Section 12, as the judge did, would not permit recovery in this case. It might bring the defendant within the eligible category of "any person who . . . sells a security," but it could not make the plaintiff into "the person purchasing such security from him." Murphy did not purchase from Rhoades & Company. A cause of action could accrue only to a plaintiff who brought himself within the definition, and that the plaintiff in this case has not done. It cannot be assumed that Congress chose the words just quoted by mistake. It would have been quite simple to use language which would impose liability for a negligent misrepresentation without a sale from the defendant. The language selected by Congress was in no way apt for that purpose. It must be construed as meaning what it specifically says —and not something else which might have been said but was not.

C. Section 12 contemplates rescission, impossible here.

Moreover, it is to be noted that Section 12 deals with rescission of a transaction. The primary right given to the defrauded purchaser is to rescind — to recover the consideration paid upon tender of the security. But rescission can only be between buyer and seller. It can never be enforced against an agent who did not have title.

McMillan v. *Arthur,* 98 N.Y. 167.
Connelly v. *Glenny,* 233 App. Div. 198.
Kinney v. *Glenny,* 231 App. Div. 311.
See also *Spiegel* v. *Beacon Participations, Inc.,* 297 Mass. 398, 418.

The result of rescission enforced by the courts must be a return to the *status quo.*

Houghton v. *Nash,* 64 Me. 477.
Sharp v. *Ponce,* 76 Me. 350.

If a purchaser could rescind against an agent, the result would not be a return to the *status quo,* but a novel transfer of title to the agent who never had it before.

See *Buck* v. *Carlisle,* 98 Ala. 580.

That Section 12 gives primarily a right to rescission is further emphasized by the fact that it gives the plaintiff a right "to recover the consideration paid for such security with interest thereon." Of course one can recover the consideration only from the person to whom it has passed. A buyer can recover the consideration only from the seller.

It is true that a right to damages likewise is given, but only where the buyer has parted with the security. The right to damages is obviously a secondary right given in a situation where the primary right of rescission would not be available. It adds nothing as far as the necessary relationship between the parties is concerned.

D. Section 12 must be strictly construed.

Finally, it must be remembered that the statute is one in derogation of the common law and so to be strictly construed.

Johnson v. *Southern Pacific Co.,* 117 Fed. 462, 466 (C.C.A. 8).
Globe & Rutgers Fire Ins. Co. v. *Draper,* 66 F. (2d) 985, 991 (C.C.A. 9).
Haggett v. *Hurley,* 91 Me. 542.
Howard v. *Howard,* 120 Me. 479.
Palmer v. *Town of Sumner,* 133 Me. 337.

It is submitted that there can be no escape from the construction which we urge in view of the language used in the section. Practical considerations of justice and hardship support the same construction and lead to the conclusion that Congress intended that construction to be adopted. The section imposes a heavy burden which it would not be reasonable to impose on a person not the owner of the security sold. If a person owns a security, *e.g.*, an issuer or underwriter, and desires to sell it, there are strong reasons for holding him to a strict standard as is done by this statute. But with the broker the situation is wholly different. On any brokered sale he can gain no more than a small commission.

In the present case the entire financial gain to Rhoades & Company from negotiating the purchase of the stock by Murphy was the net commission of $34 (Rec. pp. 135, 186, 187). The broker is not subject to the same temptation as the owner to misstate the facts. If an owner fails to consummate a desired sale, he may lose his entire investment or a material part of it. The broker, on the other hand, can lose nothing. He may not receive a commission which he might otherwise earn, but he can be no worse off than he was before. It is a matter of indifference to him whether his customer buys security A or security B. Any variation in the commission would be insignificant. But to the owner of security A it is vital that the customer buy that and not security B which someone else owns.

It is considerations such as these which have led state courts to construe state statutes similar to the Securities Act as not applicable to brokered transactions.

See *Gill* v. *Hornblower*, 294 Mass. 26.

The suggestion made by Judge Peters that the defendants although brokers are to be held liable by reason of extra-brokerage activities cannot be reconciled with the proper construction of Section 12. The judge said:

> "The ordinary brokerage transaction, merely the execution of orders to buy or sell, does not appear to be affected by Section 12. It is the extra-brokerage activity,—solicitations accompanied by false statements, —which are made the basis for a cause of action if damage is caused thereby" (Rec. p. 291).

The question is not whether the section can ever apply to any broker. Obviously it can and does where the broker owns the security and himself sells it. Rather it is whether the section can apply to anyone but an owner or his agent. Certainly the actual language of the section itself says nothing about imposing liability upon a person who does not sell because he does not own. Neither does the definition of Section 2 so enlarge it, and if it did, it still would not suffice, since that definition could have no application to the words, "person purchasing such security from him." If the section had said that any person who should make a false representation concerning a security should be liable to the person who bought the security on the strength of that representation, this appeal never would have been taken. But that is not the provision of the section. The words used by Congress are apt to apply only to a dispute between buyer and seller. The respondent did not buy from the petitioners, and consequently, we insist, the statute can have no application.

Mention is made in the petition of the fact that this case has been made the subject of a special release by the Securities and Exchange Commission and has been commented on in the Wall Street Journal in a special article published in its issue of Tuesday, September 3, 1940. There is general concern in the brokerage profession lest a statute designed to protect the purchaser of securities against fraud or negligence on the part of issuers and dealers be construed as imposing heavy risks in the conduct of the ordinary brokerage business.

The District Judge's distinction between the "ordinary brokerage transaction" and "extra-brokerage activity" (Rec. p. 291) will scarcely bear scrutiny. No broker can conduct his business without giving information to his customers on the telephone. Under this decision every customer in New Jersey who places orders with a New York broker can recover from the broker the purchase price of any security which he may buy, provided that he can induce a jury to believe that the broker said something on the telephone which turned out not to be so, or, even worse, failed to tell the customer something he would have considered material.

How the brokerage business might reorganize to protect itself against this decision cannot be predicted. Without being unduly pessimistic we may well ask why responsible persons should take the risk of losing the full purchase price of securities or a substantial part thereof, when the only possibility of gain is a fraction of one per cent of the purchase price. The rule laid down by the District Court applies not only to transactions on the open or counter market, but to those on exchanges as well. It applies also not only to an untrue statement of a material fact, but to the omission to state a material fact. Whether or not a fact not stated is to be deemed "material" must always be a nice question, but the broker's customer can always testify that he was influenced by the non-disclosure. If Congress had had any intention of imposing revolutionary changes on the commission business, it would certainly have expressed this intent explicitly in the Act, and not left it to implication from a strained and quite unnecessary construction of the statutory definition of the word "sell."

Respectfully submitted,

RICHARD WAIT,
ROBERT HALE.

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Supreme Court of the United States.

OCTOBER TERM, 1940.

EVERETT WARE CADY, ET AL.,
PETITIONERS,

v.

CLIFFORD J. MURPHY,
RESPONDENT.

BRIEF OF RESPONDENT IN OPPOSITION TO PETITION FOR CERTIORARI.

ISSUE PRESENTED TO THIS COURT.

The petitioners ask this Court to review a judgment of the Circuit Court of Appeals for the First Circuit, which court affirmed the judgment of the District Court of Maine, in which court a jury was waived. The jurisdiction of the Federal Courts is based on diversity of citizenship of the parties.

The petitioners have attempted to make it appear that a federal question of great importance is presented. In truth, the petitioners are asking this Court to review a finding of *fact* made by the District Court and affirmed by a majority of the judges of the Court of Appeals in a matter involving less than seven thousand ($7,000.00) dollars.

The petitioners state that, (Petition, page 2, lines 12 to 18):

> "The fundamental question presented is *whether a stock exchange firm which acts solely as broker for the purchaser of a security,* from whom by interstate telephone calls it has solicited an order to buy, *can be held liable as a seller of such security under Section 12(2) of the Securities Act for misrepresentation of fact regarding the security purchased.*"

The foregoing is *not* the question presented to this Court. It is only what the petitioners wish the issue was. The issue is not and never has been whether or not Section 12 (2) of the Securities Act applies to a *broker who acts solely for the purchaser.* The issue from the start has been and now is whether the Securities Act, upon the facts in this case, has enough teeth to hold the petitioners who have admittedly made false statements in soliciting an *offer* from the respondent to *buy* certain securities.

Findings of the District Court.

The District Court found *as a fact* that the petitioners acted *as agent for the seller* in the transaction in question, and solicited from the respondent not "an *order* to buy" but *"an offer to buy"* the stock in question which the petitioners' principal, E. E. Smith had for sale.

Peters, District Judge, in his opinion, Record page 291, last four lines from the bottom said:

> "The plaintiff has brought himself within the statute, Sections (12(2) and 2(3), and shown his right to recover by proving solicitation by the defendants' agent *of an offer* to buy the stock; his false material statements in regard to it, * * * *."

If the petitioners were acting solely as agent for the respondent, they would not be soliciting from their own principal an offer. They would be recommending a purchase but if the petitioners were acting (as they actually were) as agents or brokers for the owner of the security, they would be expected to do just what they did do, viz., solicit from the respondent an *offer* to buy.

On page 285, lines 22 to 25, Judge Peters further said:

> "From the somewhat conflicting evidence I consider the following facts established:
> The stock *sold to the plaintiff by the defendants,*—acting either as brokers or owners,—* * * *."

Judge Peters certainly does not say that the petitioners bought the stock as agents for the respondent. He certainly does not say that the petitioners were acting as agents for the respondent.

On page 286, lines 7 to 9, Judge Peters further said:

> "At this point it is enough to say that in numerous telephone conversations between Boston and Portland, Lynch, for his firm, solicited from the plaintiff an *offer to buy* the stock mentioned."

Certainly this quotation from the Court's opinion does not indicate that Judge Peters found that the petitioners were acting as agents for the respondent.

On page 291, lines 16 to 20, Judge Peters further said:

> "It should be noted that the statute, which applies only to interstate communications, relieves the purchaser from the common law obligation of using reasonable prudence himself and puts the burden on the *seller* to prove that he did not know and could not reasonably have known that his material statements were false."

In this paragraph Judge Peters refers to the petitioners as the "seller". Certainly, if in the opinion of the District Court the petitioners were acting solely as agents for the buyer, they would not be referred to as the *"seller"*.

Nowhere in the printed Record is there a word or a phrase that justifies the petitioners' statement that the petitioners were acting solely as the agents of the respondent. It is clear fabrication by the petitioners contrary both to the findings of the District Court, the findings of the Court of Appeals, and the record in the case.

On Lynch's (petitioners' head trader) own evidence, the District Court could not possibly draw the conclusion that the petitioners acted solely as agents of the respondent. The evidence shows that late in the afternoon of March 1, 1937, E. E. Smith of New York, who the petitioners claim was the owner of the stock, called Lynch, the petitioners' head trader, on the telephone and told him that he (Smith) had *1970*

shares of South American Utilities stock which he wanted to sell, *and asked Lynch if he could find a customer for him.* Following this conversation, Lynch called the respondent (Murphy) on the telephone *and solicited from him* not *an order* but *an offer* to buy. The respondent did not order the stock from Lynch, he simply made an offer to buy 1700 of the 1970 shares. The balance Lynch sold to other customers or bought it for his own company's account.

It was stipulated that all this was done by means of *one* telephone conversation (Record page 281). Certainly the petitioners were acting as agent for the seller in regard to the 270 shares, as the respondent had nothing to do with them, and if the whole transaction was handled in *one telephone conversation,* certainly the petitioners were acting for Smith in the entire transaction.

In the petitioners' supporting brief, page 26, lines 24 to 27, the petitioners say:

> "The evidence will support no other conclusion than that the petitioners were brokers who, *after* recommending the purchase of the shares in question, accepted and executed the respondent's order for the purchase of the shares."

The petitioners' contention apparently is that after they had misled the respondent by their false and fraudulent statements regarding the stock, as a part of their scheme they got the respondent to consent that they should act as his agents in the purchase. Thus on the petitioners' own statements during the time of solicitation of the offer for the stock, the petitioners were not the agents of the respondent but were merely asking to be employed as agents, then after they had completed their scheme and the purchaser had relied upon their representations, they became his agent to complete the purchase. What an easy means this would be for the petitioners, or anyone in their same position, to escape the effects of the Act. It was all a part of their fraudulent scheme, and at no time did they represent the respondent.

The petitioners realize that there is no justification for this petition if they were the owner or agents for the owner of the stock, or were even acting in a dual capacity as broker for both parties, but they fail to point out in their petition or supporting brief anything in the record or in the opinion of the District Court, or in the opinion of the Court of Appeals, that justifies their bold and completely unwarranted statement that the petitioners acted solely as agents for the respondent.

Findings by the Circuit Court of Appeals.

The petitioners say, Petition, page 2, lines 19 to 24:

> "There is likewise presented the question of practice whether, under the Rules of Civil Procedure, upon an appeal in a law action tried without a jury, it is competent for the Circuit Court of Appeals itself to make a finding of fact not made by the District Judge and decide the case upon the basis of that finding."

The Circuit Court of Appeals did not make a finding of fact on which its decision was based.

What the Court of Appeals actually said and what the petitioners rely on as an excuse to get this Court to pass on a question of fact will be found in *113 Fed. 2d,* 991, lines 39 to 54, where the Court of Appeals said:

> "At one point in its opinion, the Court below makes a statement of law which is broader than necessary to support the judgment rendered. It says (30 Fed. Supp. 466, 469):
> 'Whether the seller, being a broker, himself owns the security, or whether he is acting as the agent for the owner, or for the purchaser, or for both, is immaterial. If, in the course of an attempt to dispose of, or solicitation of an offer to buy a security, he makes false statements under circumstances referred to in Section 12, the purchaser is given a right of action to recover any damages he has suffered on account of the false representations.' "

The Court of Appeals further said on the same page (p. 991), lines 55 to 65:

> "We need not decide whether Section 12(2) applies to the case *of a broker acting solely for a purchaser, where the broker makes misrepresentations in the course of soliciting from the purchaser an order to buy.* Even if the version of the defendants' witness Lynch is accepted, Rhoades & Company was acting either as agent for the seller or in a dual capacity as agent for both parties, in either of which cases Section 12(2) is applicable." (italics ours)

The Court of Appeals simply and clearly said that it was not necessary for it to decide whether or not the statute applies to a broker, *who acts solely as agent for the buyer,* because Judge Peters had found that the broker acted as agent for the seller. But, said the Court of Appeals, even if the petitioners' version is to be believed, which it was not by the District Court, the petitioners were certainly acting either as agents for the seller or in a dual capacity, and in either event they are subject to the terms of the statute.

The Court of Appeals did not make findings of fact that were not found by the District Court. The most the Court of Appeals did was to review the special findings made by the District Court and said, that after viewing the evidence in a light most favorable to the petitioners, the petitioners were acting at least in a dual capacity and under such circumstances the Act applies.

The cases cited by the petitioners in their brief, pages 16-26, are not in point. These cases all hold that the Court of Appeals will not reverse the findings of the lower court unless such findings are clearly erroneous. With this we agree, but that is not the situation here. On the petitioners' own statement, the Court of Appeals has not reversed or changed the findings of the District Court,—it has only made findings which the petitioners say the District Court failed to make.

It is the duty of the Court of Appeals to uphold the judgment of the District Court if there is any evidence in the record to justify its doing so, and in this case, the Court of

Appeals found that after viewing the evidence in a light most favorable to the petitioners, the petitioners were acting at least in a dual capacity.

The respondent at all times has contended and now contends that the petitioners were either the owners of the security, or the agents for the owners of the security, at the time they made false representations to the respondent regarding the stock, and we further contend that the District Court so found. If, however, the District Court did not so find, it was the duty of the Court of Appeals to examine the record and to sustain the judgment of the District Court if there is evidence in the record to justify this, and the Court found that there was.

In *Helvering* v. *Gowran,* 302 U. S. (1927) 238, at page 245, the Supreme Court said:

> "In the review of judicial proceedings the rule is settled that if the decision below is correct, it must be affirmed, although the lower court relied upon a wrong ground or gave a wrong reason. * * * *"

In *Migeon* v. *Montana Cent. Ry. Co.,* 77 Fed. 249, at page 253, the Court of Appeals for the Ninth Circuit said:

> "We shall not stop to inquire whether any of the reasons expressed by the court were irrelevant or erroneous. The point to be decided is whether the conclusions arrived at are sustained by the evidence and the law. *Sullivan* v. *Mining Co.,* 143 U. S. 431, 12 Sup. Ct. 555."

And in *Sullivan* v. *Iron Silver Mining Co.,* 143 U. S. 431, at page 434, the Supreme Court said:

> "But, notwithstanding the technical error in this ruling, we cannot see that it wrought any prejudice to the substantial rights of the plaintiff in error, for, upon all the facts in the case, the judgment was one which must necessarily have been rendered. * * * *"

APPLICATION OF ACT.

The judge of the District Court and all three judges of the Court of Appeals held that the Act was applicable if the petitioners were the owners of the stock or the agents for the owner, when they *solicited the offer* or if they were acting in a dual capacity.

The petitioners recognize the correctness of this ruling and attempt to avoid its effects by misconstruing the findings of the two lower courts.

The District Court has found as a fact that the petitioners *solicited an offer* for the stock from the respondent. *That during their solicitations, they made false statements of a material nature regarding the stock.*

Peters, J., Record page 291, last four lines:

> "The plaintiff has brought himself within the statute, Sections 12(2) and 2(3) and *shown his right to recover by proving solicitation by the defendants' agent of an offer to buy the stock; his false material statements in regard to it,* * * * *" (italics ours)

The material part of Section 12 of the Act reads as follows:

> "Any person who sells a security * * * by the use of any means * * * in interstate commerce * * * by means of a prospectus or *oral communication* which includes an *untrue statement* of a material fact * * * shall be liable * * * * *." (italics ours)

Section 2(3) of the Act defines the word "sell" as it is to be used in the Act:

> "The term 'sale', 'sell', 'offer to sell', or 'offer for sale', shall include every contract of sale or disposition of, attempt or offer to dispose of, *or solicitation of an offer to buy,* a security or interest in a security for value; * * * *" (italics ours)

Judge Peters has specifically found facts which bring the case within the statute, that is Judge Peters has found that the petitioners *solicited an offer from the respondent to buy the stock;* that during the solicitation, the petitioners made false representations of a material nature regarding the

quality of the stock which induced the respondent to buy. These findings of fact were affirmed by the majority of the Court of Appeals and on these facts both the District Court and the judges of the Court of Appeals said the Act applies, therefore the only way this Court could reverse the findings of the lower courts would be either to disagree with the findings of fact made by the lower courts, and find, as the petitioners desire, that the petitioners acted solely as agents for the buyer in the transaction, or this Court must find as a matter of law that the Act does not apply if the petitioners were acting as agents for the seller.

Burden on Broker.

The petitioners finally urge as a reason why this petition should be granted, that the law as now drafted and interpreted by the lower courts imposes a heavy risk on a broker in the ordinary brokerage business.

This same argument was made in the District Court and in the Court of Appeals.

Judge Peters found as a fact that the petitioners' agent in his zeal to sell the stock made false representations of a material nature regarding the stock, and the innocent respondent, relying on these false statements, parted with a substantial part of his capital.

Peters, J., in his opinion, Record page 291, last four lines from the bottom said:

> "The plaintiff has brought himself within the statute, Sections 12(2) and 2(3) and *shown his right to recover by proving solicitation by the defendants' agent of an offer to buy the stock; his false material statements in regard to it.* * * * *" (italics ours)

The falsity of the statements made by the petitioners in their efforts to make a sale was so clearly proven, that the petitioners do not in this Court and did not in the Court of Appeals question Judge Peters' finding on this point.

Petition, page 5, lines 1 to 4.

The only burden the Securities Act places on anyone is *to tell the truth* and *all the truth* when selling stock, and anyone that does not do so in any business is entitled to very little sympathy.

In effect the petitioners say,—we admit that we made false statements to you regarding the stock which induced you to invest your capital, but what of it? We are not liable under the common law because you were negligent in believing us, and we hope we can escape liability under the statute by a technicality.

Certainly, it takes courage on the part of the petitioners to ask this Court for sympathy.

Judge Peters pointed out in his opinion that the Act does not apply to the ordinary brokerage transaction, *merely the execution by the broker of orders given him by the buyer,* but the Court decided it applies only to the *extra-solicitation during which the broker makes false statements regarding the security.*

Peters, J., page 291, lines 28 to 32:

> "The ordinary brokerage transaction, merely the execution of orders to buy or sell, does not appear to be affected by Section 12. It is the extra-brokerage activity,—solicitations accompanied by false statements,—which are made the basis for a cause of action if damage is caused thereby."

Cases relied on by Petitioners.

In the petitioner's brief, emphasis is placed upon *Gill* v. *Hornblower,* 294 Mass. 26, and similar cases, as supporting the contention of the petitioners. The respondent in no way disagrees with the law of *Gill* v. *Hornblower* but wishes to point out that the facts of that case are in no way analogous to the case now under consideration.

In that case, the court said, page . . :

> "On December 7, 1931, the plaintiff testatrix *went to the office of the defendants,* who were stock brokers in Boston, and

> gave them an order to buy for her five hundred shares of the common stock without par value of Electric Bond and Share Company. * * * * *The defendants were in no way interested in promoting the sale of the stock."* (italics ours)

The facts of *Gill* v. *Hornblower,* as quoted above, are to be contrasted with the language of the District Court in the present case where it said, Record page 291:

> "The plaintiff has brought himself within the statute, Section 12(2) and 2(3) and shown his right to recover *by proving solicitation by the defendants' agent of an offer to buy the stock."*

In this case the respondent did not call the petitioners, the petitioners solicited the respondent.

We respectfully submit that there is no question raised in the petition which this Court should undertake to review.

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